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Mortgage and CMO REIT Group Review

INTEREST RATES SOFTENING BUT MARKETS STILL THIRST FOR MORTGAGE REIT YIELDS

A funny thing happened on the way to Nov. 8. The expected post-election interest rate hike appears to be dissolving. August's increases in the prime and the Fed's discount rate triggered a broad fear that anti-inflation zeal would bring new rate hikes once the election is out of the way.

But September's market action is signaling a rate stall. As unemployment rises and the trade deficit sinks, the credit markets have become more positive. Fixed-rate mortgages have fallen from 10.71% on Aug. 19, shortly after the discount rate hike, to 10.35% Sept. 14. The Federal funds overnight rate has also been shaved to 8.13% from 8.38%, while Shearson Lehman Hutton's index of long-term Treasuries have advanced almost every day this month.

As a result, we have revised our credit forecast and now expect rates to remain stable, improving just slightly, through the end of the year. Another hike, however, is probably due during the first quarter of 1989.

This slightly more optimistic out-

look, however, has not changed our appetite for stocks carrying high yields. Investors are still nervous that the stock market may stagnate at best, and want equities carrying high returns. In this issue we review several solid participating mortgage REITs. **ROCKEFELLER CENTER PROPERTIES INC.**, which holds a mortgage on NYC's Rock Center, is working at a 9.1% yield that has exceptional guarantees (see p. 4). Both **TRAVELERS REIT** and **TRAVELERS REALTY INCOME** look like takeover candidates with REIT slightly favored (p.5). **MORTGAGE & REALTY TRUST's** conservative stance also generates double-digit yield (p.3).

The high yields found among CMO REITs, however, should be approached cautiously. This breed (described in detail on p. 7) has taken the REIT industry by storm and is among the few categories where underwriters can successfully sell new stock. But behind the hype, we see that this market is already being restructured. As spreads narrow sharply, **COUNTRYWIDE MORTGAGE INVESTMENTS**, **COLUMBIA REALTY** and **M.D.C. ASSET INVESTORS** are all focusing on buying existing CMO residuals rather than floating new bonds to institutions as they originally did. We see a lot of potential trauma in the CMO segment in the coming year. See p. 7-8 for our review of CMO REIT basics and selected stocks.

RANKING REVIEW ISSUE

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NOW AVAILABLE: Our revised brochure describing our money management services. Send for a free sample copy of our sister service **REALTY STOCK DIGEST**.

JOHNSTOWN/CONSOLIDATED REALTY TRUST

\$7.88 (JCT-OTC) Div. \$0.70 Yld. 8.9%
12.3 mil. shares. **RANK C**

JCT, a hybrid REIT, is now advised by Southmark Corp. Control of JCT manager Johnstown American Cos. was acquired in Mar. 1988 by SM subsidiary, San Jacinto S&L, and operations are being relocated to Dallas on Oct. 1.

Gut Issue: Will JCT get back on track and rebuild its stock price? JCT has been a high risk lender and equity investor - a policy that entails a certain amount of default but commands higher returns. However a two year string of excessive bad loans coupled with soft rental markets have put a squeeze on cash flow. In the June qtr., JCT sold two foreclosed properties for \$2.9 mil., renegotiated a \$6.4 mil. note receivable that came due by extending maturity up to nine months, but made a \$1.5 mil. provision for loan losses raising its total to \$3.6 mil.

JCT's problems have not ceased, but should subside and appear to be manageable. Assets of \$278 mil. at June 30 were mortgages, 44% or \$123 mil.; foreclosures held for sale, 3% or \$9.5 mil.; investment properties, 39% or \$109 mil.; joint ventures, 2% or \$4.5 mil.; and cash and equivalents, 10.5% or \$29 mil. Investment properties at Dec. 1987 (latest schedule available) include 11 apartment projects with 2,508 units and five commercial properties with 860,000 sq. ft.

Advice: Approach shares with caution. Dividend was cut 59% to \$0.70 but current level should be maintainable. Shares are 40% of book value but Southmark tie will hurt stock performance.

Earnings/Dividends - C (Dec. yrs.):

Yr.	OpEPS	Div.	Price*	Yld.	Rng.
85.....	1.10	1.70	20'2	-13'4	8-12%
86.....	0.51	1.70	16'2	-9'6	10-17
87.....	0.25	1.70	14'6	-6'1	12-28
88E.....	NE	0.70	8'3	-6'2	8-11z

5Yr.Gr. NM% NM% *Hi-Lo in 8ths. z-To date.

Finances - B: Debt of \$98 mil. is 0.6 times shareholder's equity of \$163.6 mil. or \$14.32/sh.; accumulated depreciation is \$0.85/sh.

Address: 2000 Powell St., Emeryville, CA 94608. (415) 652-7171. After Oct. 1: c/o Southmark, 1601 LBJ Fwy., Dallas, TX 75234. (214) 241-8787.

MERRY LAND & INVESTMENT CO.

\$7.25 (MERY-OTC) Div. \$0.80 Yld. 11%
9.40 mil. shs. **RANK B**

MERY, Augusta, Ga. based combination REIT, invests in Southeastern apartments and mortgage backed securities; it switched to REIT status in 1987 after operating as a separate real estate investment company.

Gut Issue: Would higher interest rates offset benefits from strength in apartments? MERY's \$275 mil. invested assets are 70% mortgage backed securities (or \$192 mil.); 20% properties (or \$54 mil. net after \$4.3 mil. or 46¢/sh. depreciation); and 10% corporate and government securities (or \$29 mil.). Mortgage backed securities (MBS) yield about 8.8%, offset partly by interest on \$169 mil. borrowed via reverse repurchase agreements at slightly lower rates to carry the MBS. MBS are trading at about 94.5% of cost. While not strong income contributors, MBS holdings let MERY qualify as a REIT. Other securities include \$13.5 mil. utility stocks with good yield and trading 50% over cost; \$3.2 mil. governments; and \$13.3 mil. in four Southeastern S&Ls.

Major real estate holdings are 1,487 apartments divided 38% Savannah; 34% Augusta, 28% Charleston. Average cost is \$31,850/DU. Occupancy slipped last year but has now recovered to over 90% and MERY sees rent increases within the next year. In May MERY sold a downtown Augusta warehouse (plus stock in an S&L) for 10-year notes that should add about 7¢ sh. to EPS.

Advice: At 7% over book value plus accumulated depreciation, MERY looks cheap if interest rates level or fall.

EPS/Dividends - B (Dec. yrs.):

Yr.	Op.EPS	Gains	Div.	Price*	Yld.	Range
1984.	\$0.29	.18	None	5'1-4'0	0 - 0%	
1985..	0.34	.30	"	8'3-7'5	0 - 0	
1986..	0.36	.63	"	11'2-6'2	0 - 0	
1987..	0.66	.24	.80	11'3-8'2	7.0-9.7	
1988E.	0.60	.25	.80	8'6-7'0	9.1- 11z	

5 Yr. +20% *Hi-Lo in 8ths. z-To date

MERY earned 27¢ from operations in the 6 mon. thru June, up 23%. **Finances:** Debt of \$56.9 mil. (excluding reverse repos) is 0.9 times \$60.3 mil. equity, equal to \$6.41/sh. Management owns 21%.

Address: P.O. Box 1417, Augusta, Ga. 30903. (404) 722-6756.

MORTGAGE INVESTMENTS PLUS, INC.

\$7.75 (MIP-ASE) Div. \$0.80 Yld. 10.3%
9.02 mil. shares. **RANK B**

MIP, a mortgage/joint venture REIT managed by a subsidiary of Weyerhaeuser Co., has gotten off to a fast start since coming public in 1985.

Gut Issue: Can MIP continue to hit winners in California's overbuilt office markets? MIP seeks debt/equity loans funding new construction or renovation projects, expecting to refinance these construction loans at completion of leasing. It seeks to end up with 50% of equity for which it may pay varying amounts depending upon speed of leaseup. Thus MIP wants fast rentup of projects.

Ability to refinance is MIP's acid test, and so far MIP has refinanced four projects for \$51.5 mil. and has \$14 mil. committed on a fifth project -- or 5 of 11 completed projects. MIP has committed another \$102.1 mil. to joint ventures -- \$76 mil. mortgages and \$26.2 mil. equity investment. Projects by property type are:

No.	Type	Th.SF	-Comm.:Mil.\$-		
		/DU	Mtg.	Equity	%
6	Office....	624T	\$15.1	\$12.1	27%
5	Industrial.	959T	18.3	6.1	24
3	Office/R&D.	431T	35.2	6.2	41
1	Apartment..	144DU	5.1	1.7	7
1	retail.....	20T	2.1	0.1	2
Totals....			\$75.8	\$26.2	100%

Leasing is generally going well on completed buildings at Aug. 31. Occupancy by property type: offices, 99% leased; industrial, 70%; office/R&D, 52%; apartment, 65%. One 150,000 sq.ft. industrial building is vacant, however.

A negative: Cash flow may run negative on startup projects, hurting MIP's EPS and CFS reported to Wall Street.

Advice: Shares are buy/holds for yield and potential higher returns.

EPS/CFS/Dividends - B (Dec. yrs.):

Yr.	Op.EPS	CFS	Div.	Price*	Yld.Rng.
1985..	0.40b	.45	.45	10'0-8'2	9.0-11%
1986..	0.72	.85	.85	9'7-7'1	8.6-12
1987..	0.59	.81	.80	9'0-6'5	8.9-12
1988E.	0.45	.78	.80	9'2-7'0	8.6-11z
3 Yr.Gr.	NM%	-3.0%		*Hi-Lo in 8ths	

b-From July 9, 1985. z-To date.

Finances: Debt of \$39.3 mil. is 0.5 times \$77 mil. equity, or \$8.56/sh.

Address: 6320 Canoga Ave., Woodland Hills, Cal. 91367. (818) 715-0311.

MORTGAGE & REALTY TRUST

\$18.38 (MRT-NYSE) Div. \$1.94 Yld. 10.6%
10.65 mil. shares. **RANK B**

MRT, a hybrid REIT with a large mortgage component, has recently diversified into income properties. MRT's advisor is GMAC Realty Advisors, Inc., a sub. of GMAC Mortgage Corp.

Gut Issue: Will MRT maintain earnings if interest rates begin to climb? MRT has maintained relatively stable earnings over a wide range of fluctuation in interest rates but quality investments will be harder to find in a higher rate environment. MRT's nine month operating income rose 14% to \$1.41/sh., including \$0.07/sh. of participation income. June qtr. earnings were \$0.45/sh. and cash flow was \$0.50, covering the \$0.49 dividend which seems secure for now. However, earnings have softened by \$0.02/sh. each successive qtr. during FY 1988 so far, largely because nonearning assets have risen to 6.2% of assets, vs. 4.2% in Sept. 1987.

MRT held \$478 mil. invested assets at June 30. Assets are divided 87% earning mortgages, 6% property investment, and 6.7% nonearning and low-earning loans and foreclosures. Mortgages are 45% standing loans, 24% construction/development, 4% long-term amortizing; and 23% participating loans and investments.

Advice: Hold shares for yield. With shares trading at 8% over book value, shs. give steady yield based on MRT's long track record as a careful, conservative speciality lender. Participations give inflation protection.

Earnings/Dividends - B (Sept.yrs.):

Yr.	OpEPS	OpCFS	Div.	Price*	Yield
84..	\$1.65a	\$1.65a	\$1.64	\$16'4-12'1	10-14%
85..	1.73a	1.79a	1.80	21'0-15'3	9-12
86..	2.03a	2.14a	2.13	23'3-16'1	9-13
87..	1.72	1.85	1.88	23'2-17'3	8-11
88E.	1.86	2.04	1.94	19'0-14'3	10-13z
5Yr.Gr.	+5.4%	+4.3%		*Hi-Lo in 8ths.	

a-Plus sale gains: '84-.05; '85-.05; '86-.10. z-To date.

Finances - B: Debt of \$293 mil. at June 30 is 1.62 times equity of \$180.5 mil. or \$16.95/sh. Debt is 46% short-term floating rate (commercial paper and bank); 10% medium-term revolving credit; and 44% long-term fixed rate.

Address: 3500 West Olive Ave., Burbank, CA 91505 (818) 953-7700.

ROCKEFELLER CENTER PROPERTIES, INC

\$20.13 (RCP-NYSE) Div. \$1.84 Yld. 9.1%
37.51 mil. sh. **RANK B**

RCP holds a \$1.3 bil. mortgage convertible into 71.5% interest in the Manhattan urban center of the same name. Conversion isn't permitted for 12 years, until Dec. 2000. RCP common was sold to the public in Sept. 1985 in a complex deal with massive overhanging dilution. Now RCP is using some fancy financial footwork to limit this dilution, raising two gut issues:

Gut Issue 1: Although RCP already has eliminated 29% of overhanging dilution, will repurchase costs cut cash flow and dividends? RCP has now paid \$142.2 mil. to eliminate 21 mil. shs. from the potential 72.16 mil. shares. RCP has now bought these amounts of its two convert classes:

(a) 15% of \$335 mil. current coupon (8% thru 1994, 13% thereafter till 2000, convertible at \$11.82) debentures, slicing 4.1 mil. shs. from an initial 28.3 mil. potential shs.

(b) 38% of \$952.25 mil. zero coupon debentures due 2000, initially sold at 22.58% of par to yield 10.23% to maturity and convertible into 43.86 mil. shs. at \$21.71. Repurchases eliminate 16.9 mil. potential shares.

The repurchase program has already increased the ultimate ownership percentage for outstanding shares by 8%, from 34.2% to 42.3%. To fund the \$142.2 mil. repurchases, RCP has borrowed \$366 mil. from banks, using \$224 mil. excess borrowings to buy high-grade securities whose cash flow matches bank interest payments. In this way RCP hopes to maintain cash flow, so that we expect the current \$1.84 dividend to be maintained, although the nontaxable portion (26% last year) likely will fall.

Gut Issue 2: Will debenture repurchases really boost long-term share value? Key issue here is how underlying Rockefeller Center is performing and how fast value is growing. At mid-1988, the Center was 98.2% occupied vs. 87.3% for midtown Manhattan, and new rents averaged \$42.50/sq.ft. The Center has agreed on a long-term deal assuring NBC's continued tenancy at about 91% of rents projected in RCP's offering (RSR, Feb. 12, 1988). The Center's negative

cash flow is diminishing. All this means the Center is performing more or less as projected in an overbuilt office market now showing some signs of turning back to normalcy.

These results translate into a 10% gain in appraised value to \$1.76 bil. in the first two years of operation -- or about 5% annually. When RCP came public, 6% yearly value gains were regarded as aggressive; in view of RCP's ability to maintain occupancy and rents despite midtown overbuilding, RCP's appraisers now see 4% rent gains for the next 4 years and 6% thereafter.

Based on this experience, we think it's reasonable to expect appraised value to rise about 5% yearly, equalling the last two soft years. We see three possible scenarios: (A) no further debenture repurchases; (B) repurchases doubling to about 30% and 75% of the two issues respectively; and (C) repurchases of about 50% and 100% of the two issues. We assume portfolio securities will match new debt incurred for repurchases.

RCP common bought at today's price, plus no growth in \$1.84 dividends for 12 years, would be worth the following amounts and provide total return as follows under the above three scenarios:

Scenario:	A	B	C
Common in 2000..	\$25.50	\$33.08	\$43.73
Total return.....	10.36%	11.84%	13.56%

Advice: All these returns exceed the 8.75% return appraisers say the Center would command in the open market. With a backup credit line guaranteeing liquidity and management moving to limit dilution, we see RCP shares as an opportunity to earn well above premium property returns on a world-class property. Buy on dips for very long-term.

EPS/CFS/Dividends - B (Dec. yrs.):

Yr.	Op.	EPS	CFS	Div.	Price*	Yld.	Range
1985..	0.35b	.50	.44	20'	3-17'	4	9 -10%
1986..	1.26	1.73	1.76	22'	1-17'	8	-10
1987..	1.22a	1.83	1.80	22'	4-14'	2	8 -13
1988E..	1.26a	1.82	1.84	20'	2-17'	3	9 -11z
3 Yr. +NM%		2.6%	*Hi-Lo in 8ths.				

a-Plus debt repurchase gains: '87-.11; '88-\$.13. z-To date. b-From Sept. 19.

Finances: Debt of \$825 mil. net at June 30 is 1.3 times equity of \$655 mil. or \$17.47/sh. Address: 1166 Ave. of Americas, New York 10036. (212) 841-7760.

TRAVELERS REIT

\$6.63 (TRATS--OTC) Div.\$0.68 Yld.10.3%
2.52 mil. sh. **RANK C**

TRATS, a finite life, participating mortgage REIT managed by the Keystone Funds, mutual fund unit of Travelers Corp., has experienced earnings declines after foreclosing its largest loan, a 132-room New Orleans area (Covington) Holiday Inn. Now written down to \$6.5 mil., the motel is 29% of assets.

Gut Issue: How quickly can the foreclosed hotel recover? The hotel operated at an improved 62.3% occupancy at \$48.67 average room rates since it was foreclosed in Feb. It still is showing modest negative cash flow because TRATS' operator cannot raise room rates. The location, on the north shore of Lake Pontchartrain, is sensitive to oil business. TRATS should sustain the lower 68¢ payout, even if recovery extends into 1989 or longer.

Second Issue: What will result from investor Fred Gould's block stock purchases? Gould, operating thru BRT Realty and affiliates, has bought 6.37% of TRATS at \$6.25-\$6.50 and has requested board representation. (The same group has bought a block of Travelers Realty Income -- see below.) TRATS' board has rejected Gould's request. Early this year Gould unsuccessfully tried to convert participating mortgage REIT Lincoln N.C. Realty into an intermediate term lender, to complement BRT's short-term lending, and likely has similar goals.

Meantime TRATS' other loans and leasebacks (13.83% avg. yield) perform on schedule, altho one owner is supporting loan payments. A \$4.3 mil. loan will be repaid Sept. 1989 and TRATS must decide whether to return the money to holders or reinvest.

Advice: At a 26% discount to book value and with a strong block buyer in evidence, we'd be a buyer here.

EPS/Dividends - C (Dec. yrs.):

Yr.	Op.EPS	CFS	Div.	Price*	Yld.Range
1985..	1.07	1.04	10'6-9'2	9.7-11.2%	
1986..	1.07	1.04	11'7-9'0	8.9-11.6	
1987..	0.36	0.86	9'5-4'7	8.9-17.6	
1988E..	0.65	0.68	7'4-5'7	9.1-11.6z	
5 Yr. NM%		NM%	*Hi-Lo in 8ths. z-To date		

Finances: TRATS has no debt; \$22.5 mil. equity equals \$8.92/sh. **Address:** 99 High, Boston, MA 02110. (617) 338-3460.

TRAVELERS REALTY INCOME TRUST

\$7.63 (TRIIS--OTC) Div. \$0.64 Yld.8.3%
2.13 mil. shs. **RANK C**

TRIIS, a finite life, participating mortgage REIT, is also managed by a Travelers Corp. and like Travelers REIT, has foreclosed a New Orleans area motel loan. The foreclosure has reduced earnings and dividends.

Gut Issue: With capital shrinking and a block buyer in evidence, TRIIS is an obvious takeover candidate. In 1987 and 1988 TRIIS returned to holders a total \$5.41/sh. (or 27% of the original \$20 stock price) because funds couldn't be invested to meet original yield projections. TRIIS also repurchased 132,000 shs. for \$1.1 mil. (or \$8.43/sh.), cutting equity to \$25.3 mil. or \$11.85/sh. Investor Fred Gould and BRT Realty, a short-term lender, owns 7.01% and seeks a board seat.

Finally, TRIIS took a \$3.05 mil. loss when it foreclosed the Slidell Ramada Inn in Feb. 1988; the 144-room motel is carried at \$4.7 mil. or 19% of assets. It has operated at 50% occupancy at \$38.87 avg. room rates, losing 3¢/sh. cash and depreciation since Feb.

On a positive note, TRIIS' two other investments totaling \$19.45 mil. have no problems. Despite their strength, the dividend has been cut to the present 64¢ level, which should be held. Other investments are:

Property/Location	Mil.\$	Yld.
Marriott/Green Tree, PA....	\$ 8.75	10.5%
Apartment/Lexington, KY....	10.7	10.2

Advice: Despite the steep 33% discount to June's \$11.65/sh. current value, TRIIS shs. probably have \$1 to \$1.50 premium on takeover speculation. We'd be a buyer on dips to around \$7.

EPS/Dividends - C (Dec. years):

Yr.	Op.EPS	Div.	Price*	Yld.Range
1985...	\$1.11b	\$0.80	20'0-14'5	8.0- 11%
1986...	0.79	1.60	17'6-14'3	9.0- 11
1987...	0.53	1.22c	16'3- 5'6	7.4- 21
1988E...	0.59a	0.72c	10'2- 7'3	7.0- 10z
5 Yr. NM%		NM%	*Hi-Lo in 8ths.	

a-Incl. .16 loss on invest. sale. b-From Mar. 28. c-Excl. capital return: \$3.10-5/87; \$2.31-5/88. z-To date.

Finances: TRIIS has no debt; equity of \$25.3 mil. is \$11.85/sh. **Address:** 99 High, Boston, MA 02110. (617) 338-3460.

WEDGESTONE FINANCIAL

\$7.25 (WDG-NYSE) Div. \$1.20 Yld. 16.6%
5.77 mil. shares. **RANK NR**

An aggressive Boston-based short-term lender, WDG has encountered problems recently as nonearning assets rose and the dividend was cut to reflect reduced EPS and cash flow.

Gut Issue: How long will it take WDG to turn its portfolio around and shed festering problem properties? WDG's problems start with an aggressive lending style: Loans are priced at 6% over prime and 6% commitment fee; with such rates, WDG wants only borrowers who have been turned down elsewhere but have a need for quick funds to close a real estate deal. WDG copes with an expectably higher level of problems by obtaining multiple collateral on loans (often it lends only 50% of value of this combined collateral), aggressive marketing of problem properties, and low debt.

Now problem assets have risen to over 31% of \$100 mil. investments, as follows: nonearning, 17%; foreclosures, 4%; partially earning, 11%. That's up from 21% at year-end and 11.8% a year earlier. WDG did well when it stayed close to Boston. Now over two-thirds of troubled assets require a plane ride. Examples: \$3.5 mil. in a Plant City, Fla. motel; \$8.2 mil. partially earning loan on a Kansas City office; \$2.6 mil. on an Atlanta shopping center; \$4.2 mil. on land at Candlewood Lake, Conn.; and \$3.6 mil. on Port Salerno, Fla. marina.

Advice: Avoid for now. Our sense is that these out-of-area problems will take a lot longer to shed than might be expected. The Kansas City office first became a problem in 1985 and several smaller loans have been problems for over one year. Disposition of Boston area loans may also slow.

EPS/Dividends (Dec. yrs.):

Yr.	Op.EPS	Div.	Price*	Yld.Range
1984.	\$1.01	\$0.94	9'4- 6'4	9.9-14%
1985..	1.35	1.19	10'0- 7'3	11.9-16
1986..	1.78	1.54	17'1- 9'2	9.0-17
1987..	1.79	1.79	17'2-10'4	10.4-17
1988E.	0.90	1.20	14'1- 6'6	8.5-17z

5 Yr. NM% NM% *Hi-Lo in 8ths. z-To date.

Finances: Debt of \$47.7 mil. is 0.9 times \$51.5 mil. equity or \$8.17/sh.

Address: 181 Wells Ave., Newton, Mass. 02159. (617) 965-8330.

COUNTRYWIDE CREDIT INDUSTRIES, INC.

\$6.00 (CCR-NYSE) Div. \$0.28 Yld. 4.7%
15.4 mil. shares. **RANK B**

CCR is an aggressive mortgage banker that sells originations as mortgage backed security issues but maintains a fee-based servicing portfolio.

Gut Issue: Can CCR maintain its profitability at the end of a housing cycle? We see the fundamentals behind CCR as being weak, with housing starts falling to about 1.475 mil. in 1988 and spreads having been squeezed with short-term interest rates spiking up while long-term rates flattened. CCR's FY1988 originations were up 1% to \$3.22 bil. but production from its more profitable branch network was off 33% while its use of correspondent lenders and mortgage brokers increased dramatically. May qtr. originations of \$870 mil. were a bit firmer. CCR has built an \$8.6 bil. servicing portfolio that produces recurring fee income to smooth earnings. CCR's loans are processed via a proprietary computer system linking all offices. CCR originates loans for about 0.8% (80 basis points) of principal vs. 150-200 basis points industry average. Our view: CCR earnings should hold at present levels, although further interest rate rises would hurt.

Advice: Hold shares. The U.S. is at the end of an extended housing cycle and CCR's rapid growth of mid-1980's has already reached its zenith and begins a consolidation. CCR has already navigated several economic cycles and has prepared itself for this one by decreasing its dependency on origination income by building servicing portfolio.

Earnings/Dividends - B (Feb. yrs.):

Yr.	OpEPS	Div.	Price*	Yield
'85....	\$0.28	\$0.15	\$ 5'3 - 3'3	3- 4%
'86.....	0.44	0.13	7'3 - 4'7	2- 3
'87.....	1.23	0.23	14'6 - 7'1	2- 3
'88.....	0.84	0.27	16'7 - 4'5	2- 6
'89E....	0.75	0.28	9'5 - 4'2	3- 5z
5Yr.Gr.+27.9%	+16.9%	*Hi-Lo in 8ths.		

Financial Measures - A: Short-term debt of \$539 mil. is collateralized by \$312 mil. loans held for sale. \$39.9 mil. of debt is 0.4 times shareholders' equity of \$99.5 mil. or \$6.24/sh. Management owns 24%. **Address:** 155 North Lake Ave., P.O. Box 7137, Pasadena, CA 91109. (818)304-8400. z-To date.

CMO REITS -- THE BASICS

CMO REITs are odd, confusing creatures that began coming into the market in 1985. A CMO REIT uses its equity plus big bank loans to buy (or warehouse) home loans and mortgage-backed securities. Most loans conform to FNMA or FHLMC quality standards.

The loans and securities are pledged to secure a bond-like instrument called a "collateralized mortgage obligation", or CMO. The CMOs carry a rate slightly lower than that of the underlying mortgages. The REIT's reward is the spread between the interest on the mortgages and payments to CMO holders. When you buy shares in a CMO REIT, you are buying into that planned spread which has varied from 0.4% (or 40 basis points) to over 1.0% (or 100 basis points).

CMO issuers secure agency guarantees or private mortgage insurance to attract institutional buyers. Issuers also generally overcollateralize the CMOs by pooling slightly more mortgages (usually 2%-3%) than the amount of bonds sold. Both elements protect bondholders against homeowner defaults but cut into shareholders' return.

CMO REITS have been popular among investors and their combined net worth accounts for more than a third of the equity in the REIT industry. But we have been wary -- and remain so. The mortgage securities market is tremendously volatile and even pioneers such as Salomon Brothers have gotten burned. A CMO REIT must constantly expand its portfolio, buying more mortgages to spin out new CMO issues. If the market stalls or the rules change, as they did last summer and fall, the CMO REITS can take severe hits (e.g. Countrywide Mortgage, which has ceased issuing CMOs for now--see following review). Further, the mortgage market is becoming increasingly competitive and residual spreads have been sliced in half in the last two years. Example: Lomas Mortgage Corp. spreads have fallen by about half, from 125 to 60 basis points.

We advise extreme caution. CMO REITs should be a small part of a portfolio of equity and mortgage REITs and MLPs, some of which carry high yields.

COUNTRYWIDE MORTGAGE INVESTMENTS INC.

\$6.13 (CWM-NYSE) Div.\$0.92 Yld. 15.0%
11.7 mil shares **RANK C**

CWM came public in Sept. 1985 as a CMO REIT and now holds \$1.9 bil. in home mortgages and mortgage-backed securities. CWM was sponsored by Countrywide Credit Industries Inc., a mortgage banker based in Pasadena, Calif. (p.6).

Gut issue: Has CWM's hemorrhaging ceased? CWM will not issue any CMOs for the time being, a reversal of its early aggressive operating strategy, which backfired. This should restore stability to an erratic EPS record (see EPS table below). With its link to mortgage banker CCR, the trust issued 13 series of CMOs during its first 15 months of operations. But CWM's EPS slumped 43% when commitment fees from the fixed-rate mortgage origination market ended in 1987 and fixed-rate CMO bonds became tough to sell. CWM floated just four CMO issues in 1987 and none during the first half of 1988, so fees from commitments to buy mortgages sank.

Since Dec. 1986 CWM has cut its quarterly dividend 60%, from 51¢/qtr., to 24¢ in the March qtr. and to 20¢ in the June qtr.

CWM hopefully has stabilized. Cash from an Aug. 1988 stock sale trimmed bank debt, saving about 24¢/sh. in interest expense but the additional dilution should keep EPS and dividends roughly constant. High interest rates would keep principal pre-payments down. But the spread on CWM's residuals is 0.41%, less than other CMO issuers we follow.

Advice: Avoid. CWM is underperforming healthier, less erratic CMO REITS carrying a higher yield. We don't believe CWM shares will pop up too far. The company's previous double-digit level was largely based on commitment fee income that we don't believe will return strongly anytime soon.

EPS/CFS/Dividends C (Dec. yrs.):

Yr.	Op.EPS	CFS	Div.	Price*	Yld.	Range
1985a	\$0.46	\$0.46	\$0.36	10'7-9'6	3-4%	
1986	\$2.27	\$4.52	\$2.08	19'1-10	11-21	
1987	\$1.29	\$3.73	\$1.28	16'7-4'5	8-28	
1988E	\$1.30	NE	\$0.92	9'4-5'1	10-18	

a-Six months

Finances: Book value is \$8.97/sh.

Address: 155 N. Lake Ave., Pasadena Calif. 91109. (818) 304-7523

COLUMBIA REAL ESTATE INVESTMENTS INC.

\$6.75 (CIV-NYSE) Div. \$0.88 Yld. 13.0%
6.1 mil. shs. **RANK C**

CIV is a CMO REIT sponsored in 1986 by Paine Webber. In April, the trust changed its name from Paine Webber Residential Realty Inc.

CIV was initially formed to buy jumbo mortgages generated by Paine Webber but were too large for Fannie Mae and the like. But the government securities agencies recently began accepting larger loans, sharply reducing the jumbo CMO market. So CIV is trying to buy interests in existing CMO residuals and straight mortgage securities. June qtr. EPS rose 9% to 24¢, partly because of a small stock buy-back plan.

Advice: Hold as part of a package.

EPS/CFS/Dividends - C (Dec. yrs.):

Yr.	Op.EPS	CFS	Div.	Price*	Yld.	Range
1986	\$0.88	\$0.96	\$0.73	12'5-9'1	6-8%	
1987	\$0.86	\$1.15	0.96	9'6-5	10-19	
1988	NE	NE	0.88	7'6-5'3	11-16	

Address: 10440 Patuxent Pkwy. Columbia, Md. 21044. (301) 964-8875.

LOMAS MORTGAGE CORP.

\$19.13 (LMC-NYSE) Div.\$2.60 Yld. 13.6%
8.7 mil. shares **RANK C**

LMC is a three-year-old CMO REIT sponsored by Dallas mortgage banker Lomas & Nettleton Fincl. LMC has floated 10 CMO issues backed by \$1.3 bil. in mortgages and mortgage securities.

LMC's experience demonstrates the pressures crunching CMO REITS. In Nov. 1986, LMC floated a CMO issue carrying a meaty 1.47% spread. In two issues that came out 1987, the spread was whittled to 0.54%. Overall, LMC's CMO residuals average a 0.67% spread.

Six month net income rose 3.2% to \$1.29/sh. while cash flow increased 8.7% to \$1.12/sh. LMC floated two CMO issues this year and plans two more. Since CMO REITS are yield vehicles, another interest rate hike would push LMC's price down a bit. **Advice: Hold.**

EPS/CFS/Dividends - B (Dec. yrs.):

Yr.	Op.EPS	CFS	Div.	Price*	Yld.	Range
1985a	\$0.57	\$0.43	\$0.50	20'1-19'6	9-9	
1986	\$2.14	\$2.01	\$2.14	27'6-20	8-11	
1987	\$2.54	\$2.42	\$2.52	28'5-16	9-16	
1988E	\$2.64	\$2.58	\$2.56	23'4-18'2	11-14	

a-Four months. Address: 2001 Bryan Tower, Dallas, Tex. 75201.(214) 746-7111

M.D.C ASSET INVESTORS

\$15.25 (MIR-NYSE) Div. \$2.80 Yld. 18.4%
12.6 mil. shares **RANK C**

Sponsored by Denver homebuilder M.D.C. Holdings Inc., the CMO REIT came public in Dec. 1986. MIR focuses on buying ownership interests in existing CMOs.

Gut Issue: Will MIR's recent acquisition of Guild Mortgage help or hurt? MIR bought out the San Diego-based CMO REIT July 1 in a stock swap valued at \$20.5 mil. Guild had been sliding for a year, slicing its quarterly dividend by 57% since Jan. 1987. Guild was geared to issue new CMOs every two to four months. But Guild got hit holding mortgages when interest rates spiked last summer, then the supply of fixed-rate mortgages dried up.

But MIR saw Guild as a cheap pool of existing CMO residuals. If the two companies had been combined during 1987, the merged companies' net income would have been one penny per share less than MIR's posted profit.

MIR looks pretty healthy. Six month cash flow rose 2.8% to \$1.83/sh., while net income increased 3.4% to \$1.52/sh. Costs of acquiring Guild will crimp net slightly for the second half, but won't affect payout.

The SEC is investigating MIR's purchase of mortgages from MDC. In April, investigators subpoenaed documents concerning MIR's relationship with Home-American, MDC's mortgage banking subsidiary. The commission is investigating whether MIR's purchase of \$102.3 mil. principal value of mortgages during 1987 was too sweet for the mortgage banker. The SEC wouldn't comment but MIR asserts it paid a market price for the loans. Available details of the query are sketchy, but it appears more threatening to MDC than MIR.

Advice: Hold/buy. It's pretty hard to get an 18% yield anywhere else. Higher interest rates slow homeowners' principal prepayments on mortgages and would help sustain MIR's income level.

EPS/CFS/Dividends - C (Dec. yrs.):

Yr.	Op.EPS	CFS	Div.	Price*	Yld.	Range
1987	\$2.83	\$2.20	2.55	19'2-13'6	13-19	
1988E	\$ NE	NE	2.80	16'7-14'7	16-19	

Address: 3600 South Yosemite St., Denver, Colo. 80237 (303) 773-1100